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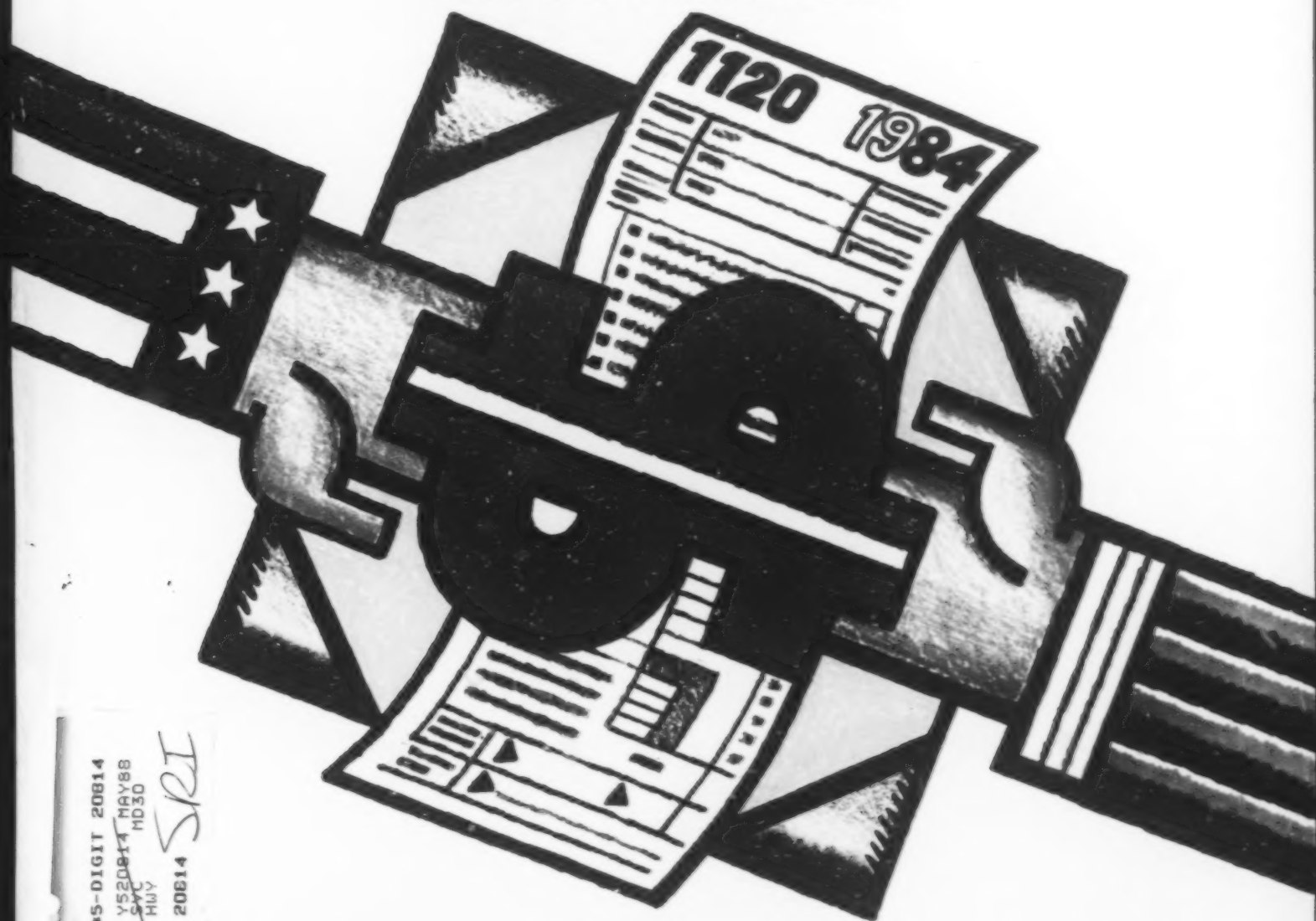
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FORTUNE

SPECIAL REPORT

THE COMING TAX INCREASE

WHO'S ON THE HIT LIST



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WINNERS
AND LOSERS
FROM LOWER
OIL PRICES

CAN
JOHN SWEARINGEN
REVIVE
CONTINENTAL ILLINOIS?

COPING
WITH THE
STRONG
DOLLAR

FORTUNE

SAAB 9000

Corporate Performance



Bob Gale's cover drawing symbolizes the tugging and hauling over taxes that lies just ahead. See page 29.

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by broadening the tax base—and business will be the prime target. The feeling on Capitol Hill that corporations are not paying their fair share has been sharpened by eye-catching reports revealing how little in taxes many big companies pay (see box at right). The average effective corporate tax rate fell from almost 22% in 1980 to about 16% in 1982. By 1983 the corporate tax was contributing only 6 cents out of every dollar paid to the Treasury, down from 12.5 cents in 1980.

The major cause of this dramatic drop-off—leaving aside the recession—has been the liberalized depreciation system and investment tax credit that Congress enacted in 1981. In 1982 and again this year, Congress scaled back those capital investment incentives. But many congressional tax writers think the breaks are still too generous. The Library of Congress's Congressional Research Service estimates that for short-lived assets, like cars and machinery, the combined effect of the investment credit and accelerated depreciation can exceed even the benefits of expensing—writing off the full cost in the year in which the investment is made. Says Ways and Means tax counsel Leonard: "The system clearly provides a corporate subsidy. And that bothers many members of Congress."

Congress remains unconvinced by arguments like lobbyist Walker's that the 1981 tax cuts helped fuel "the strongest boom in business investment since 1949." The tax writers' emerging hit list includes:

► **CAPITAL COST RECOVERY.** The 10% investment credit, which individuals and companies can take on equipment from giant machine tools to home computers, is a prime target. The Administration predicts that in 1985 the investment credit will keep about \$30 billion in potential tax revenues out of the Treasury's grasp—a calculation that does not, however, take into account any new taxable revenues generated by the protected investments. Congress won't repeal the credit outright, but could cut it back. Tax writers might also tighten up a bit more on depreciation. Hardest hit will be those profitable capital-intensive firms—like Exxon, General Motors, and General Electric—that now make heavy use of depreciation allowances and the investment credit.

► **SPECIAL BUSINESS BREAKS.** Congress may also take away a number of specialized tax incentives. Particularly vulnerable is the 25% credit for increased research and development spending. Congress enacted it in 1981, but it is scheduled to expire at the end of 1985. This year Congress refused to make the credit permanent, despite lobbying by high-tech firms, including IBM, Control Data, and Hewlett-Packard. Those compa-

A TAX STUDY BUSINESS DOESN'T LIKE

It was enough to give a business lobbyist heartburn. A labor-supported organization called Citizens for Tax Justice brought out and widely distributed in Washington a report that has whetted Congress's appetite for new tax revenues from business. The title: *Corporate Income Taxes in the Reagan Years: A Study of Three Years of Legalized Corporate Tax Avoidance*. For its study, Citizens for Tax Justice looked at 250 profitable American companies. It calculated that 128 of them paid no federal income taxes or "made money"—got refunds or other tax benefits—in at least one of the three years since passage of the Reagan tax bill. In that time the 250 companies earned profits in the U.S. of some \$57 billion.

The numbers in the study are no secret; Citizens for Tax Justice derived them from the companies' own annual reports, where tax transactions appear in the financial notes. But companies routinely (and legally) keep one set of books for the tax man and another for shareholders. For tax purposes, businesses take every break the law allows, including accelerated depreciation and investment tax credits—anything to reduce taxable income. In reports to stockholders, the emphasis goes on showing large profits by such means as stretching out depreciation. The study (see table) is based on profits as reported to shareholders and the taxes paid or tax benefits received by the companies.

Corporate tax officers queried by FORTUNE point out that the years used in the study included a wrenching recession, which crippled profits and reduced or eliminated tax obligations for many companies. They also point out that the business tax breaks in the 1981 tax bill boosted capital investment and created jobs (see page 53). When a corporation takes accelerated depreciation or other tax benefits to reduce income for tax purposes, the difference between taxes paid and the taxes that would have been due on income reported to shareholders is carried as a deferred obligation. Corporate tax directors say that Citizens for Tax Justice distorts the picture by ignoring deferred taxes. Yet any growing business will keep generating new and even larger deferrals. In some cases these deferrals become outright exemptions. In the 1984 tax act, Congress forgave about \$11 billion in deferred taxes accumulated through domestic international sales corporations by Boeing, General Electric, and thousands of other U.S. exporters.

—Craig C. Carter

MAJOR AMERICAN COMPANIES PAYING ZERO OR LESS IN FEDERAL INCOME TAX, 1981-83

COMPANY	PROFITS in millions	FEDERAL INCOME TAX in millions	TAX RATE
General Electric	\$6,527.0	-\$283.0	-4.3%
Boeing	\$1,530.0	-\$267.0	-17.5%
Lockheed	\$1,085.0	\$0	0%
General Dynamics	\$930.8	-\$70.6	-7.6%
Columbia Gas System	\$884.7	-\$94.6	-10.7%
Dow Chemical	\$776.0	-\$223.0	-28.7%
Transamerica	\$584.9	-\$86.4	-14.8%
Grumman	\$474.5	\$0	0%
American Financial	\$426.9	-\$1.9	-0.4%
Mitchell Energy & Development	\$402.8	-\$41.1	-10.2%
Greyhound	\$290.8	-\$42.1	-14.5%
Centex	\$194.2	-\$11.7	-6.0%
Champion International	\$167.0	-\$7.8	-4.7%
Singer	\$104.6	-\$12.5	-12.0%
U.S. Home	\$84.3	-\$53.3	-63.7%
TOTALS	\$14,435.5	-\$1,195.3	

Source: Citizens for Tax Justice

HOW COMPANIES ARE COPING WITH THE STRONG DOLLAR

More and more U.S. corporations have stopped waiting for the dollar to weaken and started to change how they do business—moving production offshore, selling trucks for sugar. The trick is to make changes that are reversible, in case the dollar fails. ■ by Carol J. Loomis

THE SEEMINGLY indomitable U.S. dollar, a phenomenon punishing American companies, is drastically reshaping the way that many think about their businesses. Up to now, says Lawrence A. Fox, a vice president of the National Association of Manufacturers, a lot of companies took the view that they could "ride this thing out." The dollar, they thought, would surely decline in value against other currencies, validating countless forecasts that it must. "But now," says Fox, "there is a growing feeling that Newtonian physics don't apply to exchange rates and that what goes up doesn't necessarily come down."

The companies harassed by that suspicion include three kinds of victims: U.S. multinationals get clipped with currency translation losses—a strengthening dollar deflates the profits they earn on foreign operations and reduces the value of their foreign assets. U.S. exporters find that their products cost customers overseas progressively more compared with the offerings of foreign manufacturers. U.S. manufacturers facing competition from imports find that those imports look less and less expensive to American customers. Since late 1980, when the dollar began steamrolling upward, a good many companies in its path have taken evasive action. Exporter Caterpillar Tractor, for example, has drastically cut costs and reshaped operations—though it still has losses.

The change now is that a much broader range of companies are rethinking their options, trying to develop strategies for coping with a strong dollar. Most are trying to stay

RESEARCH ASSOCIATE Rachael Grossman

flexible to avoid being whipsawed if the dollar changes course. After all, a contrarian would say the "growing feeling" that the dollar is invincible is a sure sign that it will promptly fall. The dollar was in fact looking somewhat less vigorous in early November.

Given a strong dollar, U.S. multinationals are stuck with the problem of translating weak currencies into greenbacks. When the West German mark is worth about 32 cents, as it was recently, a profit of DM 100 million translates into only \$32 million, not the \$55 million it came to in 1980. Similarly, when the British pound declines in value from \$1.40 to \$1.22, as it did this year, a U.S. company with net assets of \$140 million in Britain loses \$18 million of value.

The losses on assets have relatively minor effects. First of all, they are bookkeeping charges only, devoid of cash flow consequences unless the company chooses to liquidate the investment. Second, many of these balance sheet losses don't even affect reported profits. Using one accounting approach, for example, companies need recognize only losses on monetary assets, not fixed assets. Furthermore, a multinational can entirely eliminate its exposure to these losses in a given country by balancing its monetary assets there with liabilities, such as debt payable in local currency. If the assets shrink in value because of a strengthening dollar, the liabilities will in effect shrink also because they can be paid in units of currency that are weakening against the dollar. By loading itself up with more liabilities abroad than it has monetary assets, a U.S. multinational can actually realize currency

gains when the dollar strengthens. Rohm & Haas, the chemical manufacturer, has been doing just that.

A lot of companies, however, worry less about hedging their balance sheets these days because of a new accounting dictum, Financial Accounting Standard (or FAS) 52. Handed down in 1981, it allows many corporations to apply most gains and losses on balance sheet items directly to their stockholders' equity accounts, skipping the profit and loss statement entirely. In the equity account, these charges are called "currency adjustments," and they almost certainly go unnoticed by most shareholders. Dismissing such adjustments isn't entirely rational, though: a loss in value is a loss in value no matter where it is reported.

In the short life of FAS 52, which has known no dollar but a strong one, a good many companies have adjusted stockholders' equity for big currency losses (see table, page 119). At the end of 1983, IBM reported a cumulative currency loss for all previous years of about \$2 billion, a charge that reduced stockholders' equity from \$25 billion to \$23 billion. But because retained earnings increased in 1983 by more than the \$763-million currency loss for that year, IBM's equity still rose from 1982 to 1983. At other major companies—McGraw-Edison, an electrical equipment manufacturer, is one—a combination of small additions to retained earnings and large subtractions due to currency adjustments have caused stockholders' equity actually to decline year to year, highly unusual for corporations ostensibly making money and gaining in wealth. Perversely, a currency

THE MUSCULAR DOLLAR HAS PLENTY OF FANS ABROAD

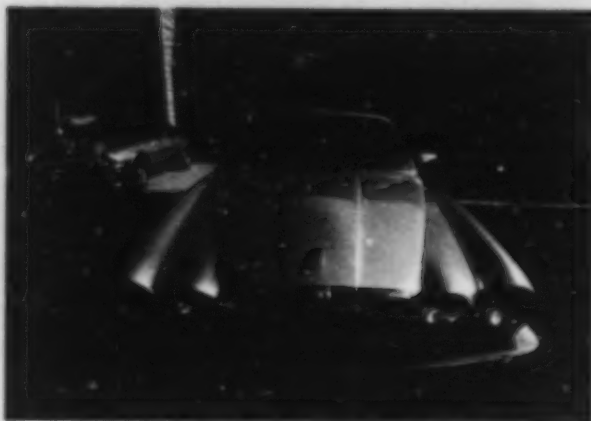
■ While U.S. multinationals bewail the strong dollar, their counterparts abroad are cheering it on. Says Takeo Miki, a general manager of the Industrial Bank of Japan, "When the yen is weak and the dollar is strong, Japanese companies in the export business are very happy." Eberhard von Kuenheim, chairman of the German automaker BMW, says wryly, "We are not exactly suffering from the strong dollar."

Compared with a few years ago, a dollar of sales is worth roughly double the amount today in marks, francs, lire, pounds, guilders, or kronor, and about 10% more in yen. European companies that don't sell goods in America but compete with U.S. companies in other markets get a boost too, because the strong dollar weakens the Americans' competitiveness. Companies that don't export much—insurance brokers and retailers come to mind—can prosper if they have a source of dollar earnings. BAT Industries, the British group that has diversified out of tobacco and owns Saks Fifth Avenue and Gimbel's, among other U.S. retail operations, is a conspicuous example. James Capel, a London stockbroker, estimates that 66% of BAT's pretax profits this year will come from America, thanks partly to the strong dollar.

One strategic decision non-U.S. companies have to make is what to do with their dollar bonuses. They can cut dollar prices to gain market share; they can hold prices but build more value into the product; they can simply pocket the money or use it for more R&D and capital investment back home. The trick is to pick the option that can, if possible, provide a lasting benefit if the dollar eventually sags.

Capital goods manufacturers have been quick to grab a price edge. Fiat's robot-making subsidiary, Comau, last spring won a big order for a welding system from General Motors, partly because of keenly competitive pricing. Airbus Industrie, Europe's challenger to Boeing's dominance, was able to use a sharp pencil in pricing the 28 planes it recently sold to Pan Am. "The dollar allows Airbus to hang in there," says a Boeing man. John Frantz, of the Boston Consulting Group, thinks one good way companies can use their dollar price advantage is to carve out market share against American competitors in third markets. The big West German chemical companies have followed just such a strategy to get a jump on U.S. competitors in commodity chemicals.

Carmakers, both in Europe and Japan, have kept their dollar prices up, sometimes even raising them. The Europeans are big in the luxury car market, which is fairly insensitive to price swings. Demand has been so strong that most manufacturers can't keep up with it. Says Edzard Reuter, finance director of Daimler-Benz, "From a marketing standpoint, it would be abso-



Jaguar turned a loss into a fat profit thanks to the dollar.

lutely wrong to respond to exchange rate variations by varying prices." Instead, the company, which sells cars in the U.S. for roughly twice the German price, is putting more into its Mercedes, including an antilock brake system as standard on all large models sold in the U.S. In Europe it remains an expensive option. While U.S. sales of most European carmakers went up nicely, revenues have soared.

U.S. sales of Sweden's Volvo, for example, will be up about 14% this year (in units), but should be up about 45% in

Swedish kronor. It's much the same story at BMW, Saab, and Audi.

Perhaps the most spectacular result has been at Jaguar, recently spun off as a private company by the British government. In the past few years, Jaguar rebuilt its American sales practically from scratch, and U.S. sales now make up over half its total business. Just how much difference exchange rate movements make is shown in calculations by Hill Samuel & Co., a London merchant bank, published in the prospectus for the sale of Jaguar stock. The bank reckoned that if the pound had stayed around \$2 rather than the \$1.50 it averaged in 1983, Jaguar would have reported a loss last year instead of a \$76-million pretax profit.

By some estimates, the major Japanese car companies are earning about 80% of their profits in the U.S. Import quotas have enabled the Japanese to avoid the price cutting they find necessary in their highly competitive home market. But the strong dollar also helps. Of all countries, Japan is its biggest beneficiary, with 30% of the country's exports going to the U.S. *Nikkei Keisai*, Tokyo's financial newspaper, calculates that every 10-yen drop against the dollar will add about \$30 million to Hitachi's pretax earnings in six months. (Recently the dollar traded at 245 yen.)

Another way non-U.S. companies can cash in is by becoming suppliers for American companies that are driven by the dollar to move manufacturing offshore. Daewoo's deal with Caterpillar Tractor to build lift trucks in South Korea is one example, as are the parts deals Detroit is discussing with such Asian automakers as Hyundai Motor in South Korea and Yue Loong Motor in Taiwan. Teksid, Fiat's metallurgical subsidiary, has long supplied cylinder heads to GM, Ford, and Chrysler, and last spring began selling hinges to Chrysler for its minivans. These deals could easily lose their shine with a drop in the dollar, though foreign suppliers do their best to write long-term contracts. In West Germany everybody from Karl Otto Pöhl, president of the central bank, on down has been urging German executives not to assume that the current situation is permanent. But that shouldn't prevent them from enjoying the ride while it lasts.—Robert Ball

loss causes a company's return on equity to look better than it otherwise would: by shrinking the equity, it causes the return on equity to rise.

On income statements, though, the strong dollar can savage profits. An upswing in the value of greenbacks during a quarter can overwhelm a rise in unit sales abroad and destroy a company's expectations for improved earnings. Those deflated profits also have pronounced cash-flow consequences. When the money sits abroad and is used to buy goods priced in dollars (such as oil), it buys less than it once did. When the profits are sent home, they add up to fewer dollars. A parent worried about a further strengthening of the dollar, in fact, will often speed up a planned repatriation of earnings, as Minnesota Mining & Manufacturing did recently with a dividend from its Australian subsidiary.

Multinationals can use the foreign currency market to hedge against fluctuations, ensuring themselves against the bad things that a strengthening dollar does to offshore profits. For example, a multinational could offset the French francs it expects to earn on operations in the next year by selling a compensatory amount of francs "forward"—that is, by contracting to deliver francs to a bank a year hence at an agreed-upon price. The contract insulates the company from adverse changes in exchange rates on the dollars at stake, though of course the estimate of earnings may prove wrong. On the other hand, the company will be shut out from realizing a gain on favorable exchange rate movements.

SOME COMPANIES consider forward contracts and other hedging devices for protecting the value of foreign profits to be essential. General Electric, for example, views the cost of hedging as necessary insurance. But Monsanto's chief financial officer, Francis A. Strobel, considers the contract prices that banks negotiate too rich to make the deals worthwhile. "For us," says Strobel, "hedging is not the answer."

Instituting price increases abroad is another form of defense. But competition may keep the lid on prices or allow only small increases. Said a recent Goldman Sachs research report: "The extraordinary strength of the U.S. dollar is burdening third-quarter earnings for several major U.S. chemical companies. Price hikes cannot offset the dollar's dramatic strength."

U.S. exporters and U.S. companies facing competition from imports have even deeper problems. When the dollar strengthens, all other factors remaining equal, the costs of the foreign producer, as expressed in dollars, will decline and it will be able to beat its U.S.

competitor on price (see box). U.S. exports will skid, imports into the U.S. will rise, and U.S. manufacturers will bleed. U.S. consumers, though, will benefit: those inexpensive imports will hold down the rate of inflation by pressuring U.S. producers to keep prices low. The American economy has been reaping that benefit on all kinds of products, ranging from potables (wine) to nonpotables (industrial chemicals) to any item using steel and copper.

U.S. exports skidded in 1982 and 1983, and this year, despite a revitalized world economy, they will be below 1981's level. Imports meanwhile will sharply exceed the 1981 total. So powerful are today's currency effects that the U.S. is importing major quantities of goods that sound like bizarre candidates for long-distance trade. Cement? Imports of ultracheap cement all the way from Spain have recently been invading the California market, making life difficult for such local producers as Kaiser Cement.

Many industries are forced by the strong dollar to think hard about the disadvantages of a U.S. location and to at least entertain thoughts of shifting their manufacturing abroad. At some corporations, the thoughts are no more than a growing "bias"—3M's description. Says its chief financial officer, Harry A. Hammerly, "We haven't made any decision to invest overseas. But margins in the products we export, such as our health care line, have suffered. I think if we were to expand capacity in that line, it just might happen overseas." At the opposite end of the action spectrum are companies that have already bitten the bullet, undertaking a big shift offshore.

Such a move works best when accompa-

	1983 CURRENCY TRANSLATION LOSS in millions	COMMON STOCKHOLDERS' EQUITY AFTER ADJUSTMENT FOR LOSS in millions
IBM	-\$763	\$32,219
Mobil	-\$553	\$13,952
Exxon	-\$539	\$39,443
Ford Motor	-\$376	\$7,545
Goodyear Tire & Rubber	-\$119	\$3,016

Low-Visibility Losses

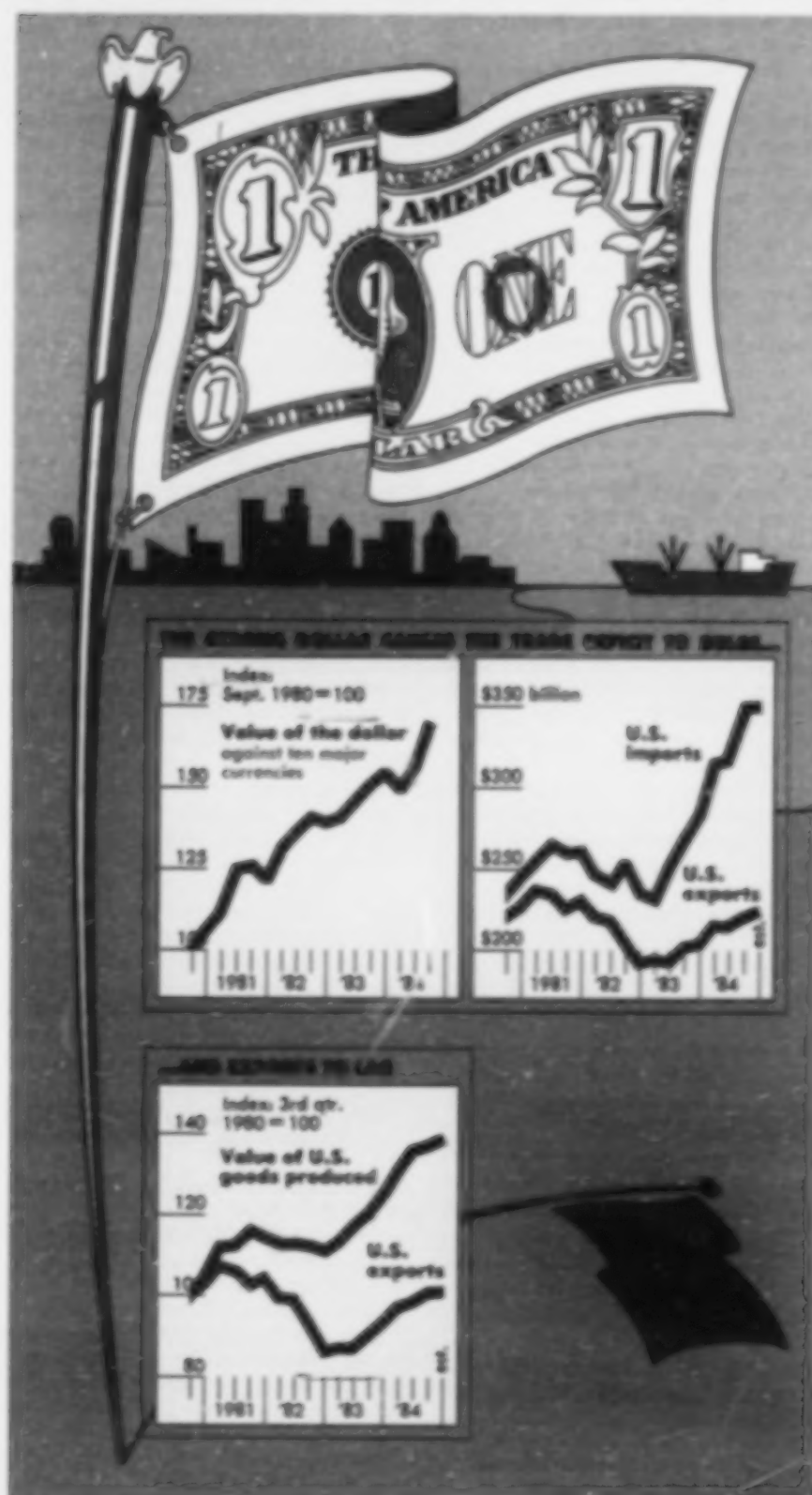
A 1981 accounting rule allows U.S. companies to apply currency translation losses directly to stockholders' equity, bypassing the income statement. Among the 50 largest industrials, these five took the biggest hits in 1983.

nied by action on the home front. Many companies assaulted by foreign competition have been making prodigious efforts to improve their U.S. productivity—closing inefficient plants, automating heavily, installing "just in time" inventory systems. "I run into some companies that aren't doing anything at all," says John R. Frantz of Boston Consulting Group. "Those are the companies that thought this problem would go away. But the well-managed companies are taking a combination approach: they're fixing up in the U.S. and they're moving overseas."

A shift in a company's manufacturing base can be accomplished in more than one way. A shutdown of capacity in the U.S. effectively does the job. A less draconian approach is a heavier "loading" of foreign plants when a given product can be manufactured either domestically or abroad. Rohm & Haas, for example, used to supply its Latin American market for water-treatment chemicals from the U.S. Today its choice of supply is Europe, where production costs less. Outright additions to facilities overseas naturally accomplish a manufacturing shift. A more flexible solution is increased purchasing of components overseas (which, when imported, will of course enlarge the U.S. trade deficit). In a recent survey of 152 manufacturing companies, the Machinery and Allied Products Institute found that 77% of them had increased their global "sourcing" (the industry's term) over the last few years. Buying abroad is, as one respondent put it, a "hot topic."

A move to manufacturing and buying overseas is not a course that charms executives tied emotionally to the U.S. These executives do not like to "export jobs" and dread being blasted by unions and politicians for doing so. Other aspects of going abroad also dismay U.S. managers: shifting production can't be done quickly. "You don't switch overnight to building tractors abroad," says a Caterpillar man. The dispersion of manufacturing to overseas sites also undercuts the economies of mass production in U.S. plants. Typically, a plant opened in Europe becomes a prisoner of national employment policies, with management retaining little flexibility to cut the work force.

And what about the egg on a company's face if it makes a wholesale shift out of the U.S. and then the dollar turns weak? Consider the example, German variety, of Volkswagen, which in the mid-1970s evaded a strong deutsche mark by beginning to produce cars in the U.S. Today Volkswagen of America is at best a marginal moneymaker, beset by other problems than the dollar—most notably, by its unappealing cars—but also burdened by the same costs that are



weighing down other U.S. manufacturers.

Frantz of BCG says the key to moving abroad is to analyze comparative production costs, U.S. vs. foreign, and then to lead the move with products that once set down in a well-chosen new location are likely to enjoy a cost advantage no matter what the exchange rate. To make a product whose manufacture consumes a lot of energy, a company might, for example, go to Canada, which is going to be forever blessed with cheap hydroelectric power. The costs of labor are more changeable, but Frantz expects that Korea, Taiwan, and Brazil will have comparatively low wages for a long time—and thus also have a near-permanent cost advantage. Costs in the Far East explain why U.S. auto companies have been heading there. GM has a joint venture to build cars in Korea, Ford is considering expansion of its plant in Taiwan, and Chrysler is talking to both countries about manufacturing possibilities.

Frantz gives high marks for moving abroad to Ingersoll-Rand, which with BCG's advice began restructuring its global strategies in 1982 after a new man, James E. Perella, took over international operations at the machinery maker. The company was then making about 75% of the products it sold internationally in U.S. plants. Now the proportion is below 60% and declining.

Ingersoll-Rand has shied from building plants overseas—it has, in fact, closed some it judged inefficient. Says a Perella lieutenant, D. King Cunningham: "You don't want to be in the position of making very basic decisions and then having the dollar swing." Ingersoll-Rand did build a compressor plant in Avellino, Italy. "We are confident," says Cunningham, "that the Italian lira will forever be soft against the dollar."

In the U.S., meanwhile, Ingersoll-Rand has closed 15 plants, consolidated a lot of offices, and renegotiated its labor contracts, securing concessions from workers. The company's U.S. employment has dropped from 34,500 in 1981 to 23,300 now. Including a \$40-million charge for the restructuring going on internationally, the company last year took a \$138-million write-off that bumped it into the red but gave it hopes, according to its 1983 annual report, of emerging "a stronger, more resourceful company." It has at least emerged profitable: earnings for

The Dollar's Devilry

Since late 1980 the U.S. dollar has appreciated 70% against a trade-weighted average of ten other major currencies. In 1984 the trade deficit in merchandise could exceed \$120 billion.



KOSHER 1/10/84

A stark reminder of import woes, this worldwide parts distribution center Caterpillar started building in 1982 sits abandoned—for now—in Illinois.

1984's first three quarters were \$36 million (on \$1.8 billion in sales), around 30% of what they were back in 1981.

At Caterpillar the losses—\$177 million in the first nine months on \$4.9 billion in sales—by no means stem from the dollar alone. The construction equipment market worldwide has been weak. Cat also concedes that it got pretty complacent a few years back. It would be locked in strenuous battle with its major competitor, Japan's Komatsu, even if the dollar were at its 1980 level. Still, the dollar's damage is mighty. Since 1981, Caterpillar has cut its U.S. employment from 86,000 to 63,000, announced the permanent closing of five U.S. plants, and waged an efficiency drive that after adjustment for inflation has cut 14% from the company's costs. Says Chairman Lee I. Morgan: "The organization has developed skills of cost reduction it didn't know it had." But since 1981, the yen has weakened about 11%, offsetting most of Caterpillar's cost improvement. Add

efficiency gains that Komatsu itself has been making and you end up with Caterpillar losing ground in the cost competition.

CATERPILLAR wants to get eight more percentage points of cost improvement by the end of 1985, and it broods a lot about the dollar. Says Executive Vice President Donald V. Fites: "Let's face it. If you've got 75% of your assets in the U.S. and 50% of your sales outside it, and the dollar's strong, you've got problems." Caterpillar has said it will "shop the world" for components, about 70% of which the company now produces internally (against Komatsu's 30%). More than 50% of the pistons the company uses in the U.S. already come from abroad, mainly from a Brazilian company. Some work previously done by Cat's Milwaukee plant has recently been moved to a subsidiary in Mexico.

Caterpillar is also stopping most production of lift trucks in the U.S. and in a few

months will begin importing a new line—complete with Cat's yellow paint and logo—from Korea's Daewoo. The shift to Daewoo was dictated by the economics of lift trucks: in excess supply and highly price-sensitive, they are made chiefly by the Japanese, whose production costs Cat simply couldn't match in the U.S. At Daewoo, a small contingent of Cat employees will guard quality and have the final say on what product can be shipped. Even so, the move to trust an outside manufacturer—in a newly industrialized country yet—is a radical departure for Caterpillar. "Five years ago," says Lee Morgan, "this project would not even have received consideration."

The plant closings are perhaps not over at Cat. Don Fites talks of "excess capacity" in the U.S. and of the need to disperse more manufacturing overseas. Right now Cat has dual sources, domestic and foreign, for some products, and it expects to set up dual sources for others. These will allow Cat to



Instead of exporting *had linens to Europe, West Point-Pepperell cuts costs by shipping cloth to this factory in Ghent, Belgium, for finishing.*

"load" the plant that offers the best economies of production, given exchange rates at any moment. But these arrangements also create manufacturing redundancies and impede the move to cut costs. Morgan says you just have to live with this problem for the sake of flexibility.

Cat has also set up Caterpillar World Trading Corp., which will try to develop incremental sales through countertrade. In such deals, possibly involving a dollar-starved Latin American country, Cat will get paid in some commodity other than cash—perhaps an edible currency like bananas. The company will then have the job of converting the bananas into cash, its ultimate profit depending on how slippery that job turns out to be.

Other U.S. companies have also leaned on countertrade deals to wrestle business from foreign competitors. Mack Trucks, whose once thriving export business has all but disappeared, recently sold trucks to the Dominican Republic through a distributor, who then

in effect got paid in sugar. Mack's president, John B. Curcio, says the deal didn't make that much money—"but you have to keep trying," he adds, "or you will lose your customers to the competition."

MARKETING persistence has become a way of life at Omark Industries, a Portland, Oregon, manufacturer of chains for chain saws that its president, John L. Warne, calls "the IBM of this business." Omark has historically exported 40% of its output. It faces a rugged German competitor, Stihl. "Our first decision when the dollar went up," says Warne, "was to maintain our world market at all costs, even at the expense of our profits." The company has not raised its prices for 3½ years and its profits have dropped 42% since 1980. But if the dollar ever turns, Stihl had better watch out because Omark has seen this crisis as a reason to bear down on productivity. It is both fix-

ing up things internally and shifting production out of the U.S. A Canadian plant that makes chains is now running at 100% capacity. The Portland plant, whose production costs are 25% higher, is down at 80%. Omark has also sent 65 of its top management to Japan to study manufacturing methods and quality control procedures there, and the company has installed many of these techniques in its plants.

The productivity improvements being made at America's Omarks are a brighter side of the strong dollar. They are a way of coping that holds promise for the future and that is infinitely preferable to the cop-out of protectionism. But it would be wrong to be pollyannaish about the other side of the strong dollar—the geographical imperative American companies feel to move manufacturing overseas. For all their attempts to stay flexible, these companies are making changes that will be hard to undo should the dollar begin its long-awaited decline. ■